

**CALIFORNIA STATE BOARD OF EQUALIZATION**  
**APPEALS DIVISION BOARD HEARING SUMMARY**

In the Matter of the Claim for Refund	)	
Under the Sales and Use Tax Law of:	)	
ELIZABETH SHUTTERS, INC.	)	Account Number SR EH 100-565493
Claimant	)	Case ID 538185
	)	Colton, San Bernardino County

Type of Business:           Manufacturer and installer of customer shutters

Claim Period:                10/01/05 – 09/30/08

<u>Item</u>	<u>Claimed Refund</u>
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Over-reported tax on construction contracts	Unstated
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The Board heard this matter on May 31, 2012, and ordered that the claim for refund be denied. Claimant filed a timely petition for rehearing, which the Board granted on December 18, 2012. The second Board hearing was scheduled for April 2013, but was postponed at claimant's request because of a scheduling conflict.

**UNRESOLVED ISSUE**

**Issue:** Whether the amount of overpaid tax is greater than the amount established by audit. We find that the actual overpayment has already been refunded, and that no further refund is warranted.

Claimant is a manufacturer of custom shutters for sale to homeowners and prime contractors. It also furnishes and installs the shutters under lump-sum construction contracts. During the period October 1, 2005, through June 30, 2007, claimant collected sales tax reimbursement on its entire lump sum contract price for construction contracts, and reported the full amount of those contracts as taxable retail sales. Thus, for that period, claimant had collected excess tax reimbursement, which it had reported to the Board. Claimant then became aware that, for its lump-sum construction contracts, tax applies to the cost of materials and to the selling price of fixtures, rather than to the full contract amount. Accordingly, claimant stopped collecting sales tax reimbursement with respect to its lump-sum construction contracts and, for the period July 1, 2007, through September 30, 2008, computed the taxable measure it reported for those contracts by applying 52 percent to the total contract amount, a percentage it had computed based on a review of a few contracts.

1 In the audit, the Sales and Use Tax Department (Department) found that the shutters were  
2 fixtures, and for the period July 1, 2007, through September 30, 2008, the retail selling price of the  
3 fixtures as computed by the Department exceeded claimant's reported taxable measure for contracts by  
4 \$1,008,259. Before a Notice of Determination was issued, claimant protested the audit findings, and  
5 the Department prepared a revised audit. In the revised audit, the Department made various revisions  
6 to its computation of the taxable measure related to claimant's construction contracts. For example, in  
7 its revised computation of the selling price of shutters, the Department did not include the general and  
8 administrative overhead costs. Also, the Department found that, while the shutters used in windows  
9 are fixtures, the framing, shutter doors, and shutter wall partitions should be regarded as materials,  
10 with the applicable tax measured by cost rather than retail selling price. Using its revised computation  
11 of taxable measure, the Department found that claimant had overstated its reported taxable measure  
12 related to construction contracts by \$233,347 for the period July 1, 2007, through September 30, 2008.  
13 After offsetting understatements in other areas, there remained a net overpayment, and the Department  
14 has thus issued a refund of \$10,702.12 for the audit period.

15 Claimant argues that the amount of overpayment was greater than the amount refunded because  
16 the shutters it manufactures and installs should be classified as materials, rather than fixtures, with tax  
17 due on the cost of materials rather than on the selling price of the shutters. Claimant asserts that the  
18 relevant question to answer in deciding whether the shutters are fixtures or materials is the ease and  
19 relative cost of detachment of the shutters and re-attachment to other realty. Claimant states that it is  
20 impractical to remove the shutters from the realty because of the damage that would result to both the  
21 shutter and the realty. In addition, claimant disputes the Department's comparison of its shutters to  
22 Venetian blinds, arguing that the shutters require installation by a professional with significant  
23 experience. In its petition for rehearing, claimant also asserted that the "cabinet rule" should be  
24 applied to determine whether the shutters were fixtures or materials.<sup>1</sup>

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26 <sup>1</sup> In short, under the "cabinet rule," when 90 percent or more of the total direct cost of labor and material in fabricating and  
27 installing a cabinet is incurred prior to affixing that cabinet to the realty, then that cabinet is a fixture. (Cal. Code Regs., tit.  
28 18, § 1521, subd. (c)(2).) Where the percentage is less than 90%, the cabinet is regarded as having been installed as  
materials.

1 In relevant part, California Code of Regulations, title 18, section 1521, subdivision (a)(4)  
2 defines “materials” as tangible personal property affixed to realty that loses its identity to become an  
3 integral and inseparable part of the real property. In contrast, subdivision (a)(5) in relevant part defines  
4 “fixtures” as items accessory to a building or structure that do not lose their identity as accessories  
5 when installed. Here, while the shutters may not be removable without some damage to the window  
6 frame or the shutter itself, the shutters are merely accessory, not necessary, to the integrity of the  
7 window, the window opening, or the real property surrounding them, and maintain their identity as  
8 shutters after installation. Accordingly, the shutters meet the definition of fixtures as defined in  
9 subdivision (a)(5), and do not qualify for the definition of materials as defined in subdivision (a)(4).

10 Regarding claimant’s assertion that the “cabinet rule” should be applied to determine whether  
11 the shutters were fixtures or materials, we note that claimant furnished and installed shutters and often  
12 also furnished and installed framework into which the shutters were installed. There is no dispute that  
13 the framework constituted materials. Claimant believes that the cost of the labor and materials to  
14 furnish and install the framework should be considered, along with the cost of the labor and materials  
15 to furnish and install the shutters, to determine the percentage of the total cost of fabricating and  
16 installing the shutters that is incurred prior to affixing the shutters, which should then be used to  
17 determine whether the shutters are fixtures or materials. However, just as the cost to furnish and install  
18 a necessary wall is not combined with the cost to furnish and install a cabinet attached to that wall to  
19 determine if the cabinet is a fixture, the cost to furnish and install framework is not combined with the  
20 cost to furnish and install a shutter attached to that framework to determine whether the shutter is a  
21 fixture. If the cabinet rule were applicable here, it would be applicable to the shutter itself, not to the  
22 shutter *and* the framework combined. In other words, the shutters are discrete items that were  
23 prefabricated prior to installation at the jobsite. Accordingly, even if the cabinet rule were applicable  
24 here, the shutters would still be properly classified as fixtures. Accordingly, we find that the shutters  
25 installed by claimant were fixtures, and that no further refund is warranted.

#### 26 OTHER MATTERS

27 None.

28 Summary prepared by Deborah A. Cumins, Business Taxes Specialist III